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In the Supreme Court of the United States

OCTOBER TERM, 1970

No. _____

CESAR E. ALVAREZ and ANA I. ALVAREZ,
Petitioners,

vs.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The petitioners, Cesar E. Alvarez and Ana I. Alvarez, respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fifth Circuit entered in this proceeding on September 1, 1970.

OPINION BELOW

The opinion of the Court of Appeals, not yet reported, and of the District Court for the Southern District of Florida appear in the Appendix hereto.

JURISDICTION

The judgment of the Court of Appeals for the Fifth Circuit was entered on September 1, 1970. The petition for certiorari was filed within 90 days of that date. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

QUESTIONS PRESENTED

Whether confiscation by the Cuban government of rental property used in trade or business in return for unsecured monthly indemnification payments, which are paid and received until a subsequent divesting enactment, constitutes a taxable loss of the underlying rental property in the year in which the right to receive indemnification payments is extinguished.

STATUTORY PROVISIONS INVOLVED

1. United States Code, Title 26

§ 165. Losses

(a) General Rule. — There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.

• • •

(c) Limitation on losses of individuals. — In the case of an individual, the deduction under subsection (a) shall be limited to —

(1) Losses incurred in a trade of business . . .

2. Code of Federal Regulations, Title 26

§ 1.165-1(d). Year of deduction.

(2)(i) If a casualty or other event occurs which may result in a loss and in the year of such casualty or event, there exists a claim for reimbursement with respect to which there is a reasonable prospect of recovery, no portion of the loss with respect to which reimbursement may be received is sustained, for purposes of Section 165, until it can be ascertained with reasonable certainty whether or not such reimbursement will be received . . .

STATEMENT OF THE CASE

Cesar and Ana Alvarez, as husband and wife, filed income tax returns for the years 1961, 1962, and 1963. In 1964 and 1966 they filed claims for refund asserting over-payments for the taxable years 1962 and 1963. These claims were disallowed by the Commissioner of Internal Revenue.

After exhausting the administrative remedies available to them, Mr. and Mrs. Alvarez successfully brought suit for the recovery of the taxes paid in the United States District Court for the Southern District of Florida, under the provisions of 28 U.S.C. § 1346. Judgment was entered for Mr. and Mrs. Alvarez on July 10, 1969. The Circuit Court of Appeals for the Fifth Circuit reversed in an opinion in direct conflict with the opinion of the United States District Court for the Northern District of Illinois in the consolidated cases of *Beltran v. United States* and *Onetti v. United States*, reported at 69-2 USTC ¶ 9649, appeal pending, United States Court of Appeals for the Seventh Circuit. An appeal from a Tax Court decision (*Luis and Alicia P. Bosch v. Commissioner*, CCH T.C.M. 1970-66) of a very similar Cuban confiscation case is pending in the Fifth Circuit Court of Appeals.

The Fifth Circuit opinion in the instant case itself clearly invites guidance from the Supreme Court; the Circuit Court carefully drew attention to the fact that its decision was directly contrary to the result reached in another Federal court.

Moreover, the far-reaching significance of its departure from established tax law doctrine, as well as the

serious conflict it has produced in judicial treatment of Cuban loss cases, makes the Fifth Circuit decision unusually appropriate for Supreme Court review. The tax treatment of Cuban expropriation losses in itself is an issue of significance. However of much greater importance is the impact of the Fifth Circuit's decision upon all tax loss cases in which there is a claim for reimbursement — a very common situation.

Prior to June 6, 1961, Cesar Alvarez was a Cuban national residing in Cuba. He owned improved business property in Camaguey, Cuba, which was rented to several tenants for commercial purposes.

On October 14, 1960, the revolutionary government of Cuba enacted the Urban Reform Law. This enactment outlawed and declared null and void all contracts for the renting of urban property, and provided a means by which the tenants could "purchase" the premises at a fixed price to be paid in monthly installments.

Under the specific provisions of the Urban Reform Law, Provisional Urban Reform Councils authorized contracts of sale with installment payments of the sales price computed by means of a formula based on the age of the buildings involved. The tenant paid the government, and the government paid the former owner.

Mr. Alvarez received installment obligations totaling $22,400 for his share of the improved business property, payable $200. per month for a period of nine years and four months. The only requirement for receiving indemnification payments was the making of a declaration of ownership. Mr. Alvarez made the necessary declaration

and monthly indemnification payments were made to his order. These payment checks were delivered to his bank in Cuba, where between October 14, 1960 and June 6, 1961, the checks were picked up and cashed.

Because of the unstable political situation in Cuba, Mr. Alvarez left that country and came to the United States to join his family on June 6, 1961. He became a resident alien on July 6, 1961, thus making his income taxable in the same manner as a citizen of the United States. Even after leaving Cuba, installment payments for the purchase of his rental property were made to his order, delivered to Mr. Alvarez' bank in Cuba, and were available to him in Cuba.

On December 5, 1961, the Cuban government enacted Law No. 989, which confiscated all assets left in Cuba by those who did not return within a stated period. Mr. Alvarez did not return and whatever property rights he then had in Cuba were confiscated.

When Mr. Alvarez departed Cuba for the United States in June of 1961, he did not forfeit any rights that the Urban Reform Law granted to him in exchange for his confiscated property. He retained the title to the property, as well as the right to receive installment payments on the purchase price. This claim for reimbursement subsisted until December 5, 1961, when it was included within the purview of the Cuban confiscation law of that date.

In his Findings of Fact and Conclusions of Law, the trial judge determined that Mr. and Mrs. Alvarez were entitled to a loss deduction under Section 165 of the Internal Revenue Code because they had proven by a pre-

ponderance of evidence that they owned the property for which the loss was claimed; that they did not sustain the loss on the property at or before the time of their departure from Cuba on June 6, 1961; that they were resident aliens of the United States at the time the loss occurred on December 5, 1961, when their right to indemnification for their property was taken; that the character of the loss took on the nature and character of the asset from which the right to indemnification arose; that the expropriated property was property used in trade or business; and that Mr. and Mrs. Alvarez were entitled to a business loss which could be carried back and carried forward as a net operating loss in accordance with the provisions of the Internal Revenue Code, Sections 165, 172 and 1231. Final Judgment was thereafter entered on July 10, 1969, by which Cesar Alvarez and Ana Alvarez recovered from the United States of America sums paid as taxes for the calendar years 1962 and 1963.

The United States Court of Appeals for the Fifth Circuit reversed the trial court, holding in effect that that which was confiscated on December 5, 1961, was an indemnification right, a nonbusiness capital asset, unrelated to the business property for which it had been received. Under the applicable Code provisions, such a loss would be deductible, if at all, in 1961, and could not be carried forward to the years 1962 and 1963.

The opinion of the Circuit Court of Appeals for the Fifth Circuit, unsupported by citation to authority, concludes that to characterize the loss which was sustained by Alvarez as a trade or business loss " . . . is not the better view."

REASONS FOR GRANTING THE WRIT

1. THE DECISION BELOW RAISES SIGNIFICANT AND FAR REACHING PROBLEMS CONCERNING EFFECTIVE ADMINISTRATION OF THE TAX LAW.

The Fifth Circuit's opinion in this case is not only of great importance to the large number of Cubans who have established residence in the United States and who have made claims similar to those involved herein, but the implications of the decision extend far beyond the field of foreign expropriation losses. This decision cuts across the entire spectrum of business activity, and basically affects any situation involving the timing and characterization for Federal income tax purposes of a partially or fully compensable loss. The doctrine set forth by the Fifth Circuit purports to transform a business asset into a non-business asset where a claim for compensation comes into existence. Such a doctrine would necessarily be applicable in any case where a compensation claim is ultimately rejected. It would deny a tax deduction for a trade or business loss, and preclude applying such a loss to income earned in subsequent years, both of which tax practices are otherwise allowable under the Code and regulations. To permit the decision of the Fifth Circuit to stand would be to permit a novel and disruptive development in the law of income taxation without the slightest support in reason, the Internal Revenue Code, case law, or administrative ruling. For these reasons the decision of the Fifth Circuit in this case presents questions whose resolution will have immediate importance far beyond the particular facts and parties involved.

2. THE ISSUE INVOLVED IN THE DECISION BELOW IS INVOLVED IN OTHER CASES PENDING IN LOWER COURTS AND IN INNUMERABLE ADMINISTRATIVE PROCEEDINGS, THEREBY MAKING A DEFINITIVE RULING BY THIS COURT DESIRABLE.

The Fifth Circuit's opinion in this case recognizes that there are decisions by other courts involving questions similar to those presented, including cases in which it has been held that losses similar to those sustained by Mr. Alvarez were trade or business losses. One of the cases mentioned is presently pending before the Fifth Circuit Court of Appeals, and another is presently pending before the Court of Appeals for the Seventh Circuit. In addition, the decision rendered below is obviously an important decision involving many individuals who will be making claims for Cuban expropriation losses as well as others claiming losses where a claim for reimbursement has been extinguished.

3. THE DECISION BELOW CONFLICTS WITH THE DECISIONS OF OTHER COURTS AS TO THE PROPER INTERPRETATION OF SECTION 165 OF THE INTERNAL REVENUE CODE, AS WELL AS THE CONTROLLING ADMINISTRATIVE REGULATIONS PROMULGATED BY THE ADMINISTRATIVE AGENCY CHARGED WITH ITS ENFORCEMENT.

While the holding of the Fifth Circuit in this case does not presently conflict with that of another Court of Appeals, it is in direct conflict with the 1969 decision of the United States District Court for the Northern District of Illinois in the consolidated cases of *Beltran v. United States of America* and *Onetti v. United States of America*, supra, appeal pending, United States Court of Appeals for the Seventh Circuit. Furthermore, the decision rendered below is in direct conflict with Section 1.165-1(d)(2)(i) of the Code of Federal Regulations, 26 C.F.R. § 1.165-1, which specifically states that a loss arising out of the destruction or taking of property, where a right of reimbursement comes into being at the time of such destruction or taking, is sustained for tax purposes when and only when it is determined with reasonable certainty that the claim for reimbursement will not be satisfied.

This regulation has been approved by numerous decisions of the United States Tax Court, in particular that of *Harry J. Colish*, 48 T.C. 711 (1967). By divorcing the trade or business attribute of the confiscated property from the right of indemnification received in its place, the decision of the Fifth Circuit is so inconsistent in theory with the provisions of the applicable Treasury Regulation as to leave its intent and meaning in a complete state of confusion.

CONCLUSION

For these reasons a writ of certiorari should issue to review the judgment and opinion of the Fifth Circuit.

Respectfully submitted,

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APPENDIX

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

October Term, 1969

No. 28789

D. C. Docket No. CA 68-1-EC
CESAR E. ALVAREZ, ET UX,
Plaintiffs-Appellees,

versus

UNITED STATES OF AMERICA,
Defendant-Appellant.

Appeal from the United States District Court for the Southern District of Florida

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Before JONES, WISDOM and COLEMAN, Circuit Judges.

JUDGMENT

This cause came on to be heard on the transcript of the record from the United States District Court for the Southern District of Florida, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby reversed; and that this cause be, and the same is hereby remanded to the said District Court in accordance with the opinion of this Court.

It is further ordered that plaintiffs-appellees pay to defendant-appellant, the costs on appeal to be taxed by the Clerk of this Court.

Issued As Mandate: September 1, 1970

IN THE
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 28789

CESAR E. ALVAREZ, ET UX,
Plaintiffs-Appellees,

versus

UNITED STATES OF AMERICA,
Defendant-Appellant.

Appeal from the United States District Court for the Southern District of Florida

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(September 1, 1970)

Before JONES, WISDOM and COLEMAN, Circuit Judges.

JONES, Circuit Judge: Cesar Alvarez and his wife, Ana, filed income tax returns for the years 1961, 1962 and 1963. In 1964 and 1966 they filed claims for refund, asserting overpayments for the taxable years 1962 and 1963 in the amounts of $65.00 and $416.00. The Commissioner of Internal Revenue disallowed the claims and this action

was brought in the district court to recover the amounts paid. Ana Alvarez was a party to the suit and is a party here because, as the wife of Alvarez, she joined in the filing of joint returns. The district court decided the case in favor of the taxpayers and entered a judgment for them. The United States has appealed.

Prior to 1961, Cesar Alvarez was a Cuban National residing in Cuba. He owned improved business property in Camaguey, Cuba, which was rented in several parcels to different tenants. On October 14, 1960, the Cuban Government enacted the Urban Realty Reform Law. By this law, the State of Cuba took almost all urban rental property, including that of Alvarez. The law provided for indemnification to the former owners of rental property in an amount established by formula and the only requirement for indemnification was the making of a declaration by a former owner of the property which he owned and on which he collected rent.

Alvarez made the necessary declaration and was awarded a total indemnification of $22,400.00 payable at the rate of $200.00 per month. He received eight monthly installments from October 31, 1960 to May 31, 1961. On June 6, 1961, Alvarez left Cuba and entered the United States. Prior to this date he had made several trips to the United States to visit the members of his family who had moved to Florida in November 1960. Alvarez became a resident alien and acquired the status of a United States taxpayer on July 6, 1961. Monthly indemnification checks were made out to Alvarez and delivered to his bank in Cuba until December 1961. These installments were not received by Alvarez since his physical presence was necessary to obtain the checks.

The Cuban Government, on December 5, 1961, enacted Law No. 989 providing for the total confiscation of property in Cuba, of whatever nature, owned by Cuban Nationals who failed to return to Cuba within a designated time. Alvarez did not return and thus he ceased to be entitled, under the Cuban law, to receive payments of indemnification, both those which had accrued and thereafter to accrue, for the 1960 taking of his property.

In his claims for refund, Alvarez alleged that his interest in the property owned by him in Cuba had been taken on December 5, 1961, after he had become a resident alien, and that this loss was deductible under Section 165 of the Internal Revenue Code of 1954[1] as a loss of property used in his trade or business and that he was entitled to a net operating loss carryover[2] to 1962 and 1963. The Government contends that if there was a loss, it was sustained by Alvarez before he became a resident alien and it is therefore not an allowable loss within the meaning of Section 165 of the Internal Revenue Code. The Government takes the position that because of the difficulties which Alvarez would encounter in realizing upon his right to indemnification after leaving Cuba and before becoming

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[1]The relevant portions of this section of the Code provide as follows:

"(a) General Rule. — There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.

. . .

"(c) Limitation on Losses of Individuals. — In the case of an individual, the deduction under subsection (a) shall be limited to —

(1) Losses incurred in a trade or business . . . "

28 U.S.C.A. § 165(a) and (c)(1).

[2]See 28 U.S.C.A. § 172.

a resident alien, he had lost the right which would have been open to him if he could have presented himself at his bank in Cuba to receive and cash the indemnification checks. If Alvarez sustained a loss of his Cuban property and property rights before he became a resident alien, the loss would not be allowable as a deduction.[1]

Although it would have been necessary for Alvarez to return to Cuba in order to obtain and cash the indemnification checks issued to him and sent to his bank, the right existed and was recognized by the Cuban Government, which was performing its undertaking to make payments. The checks which had been issued were payable to him and the right of indemnification continued. This was not, in the existing situation, any condition or state of hopelessness of recovery so as to constitute, within the meaning of the tax law, a loss of his right to indemnification. See *Estate of Fuchs v. Commissioner*, 2d Cir. 1969, 413 F.2d 503; *Harry J. Colish v. Commissioner*, 48 T.C. 711. At the time Alvarez became a resident alien he had, in our opinion, property rights consisting of the obligations of the Cuban Government in its promise of indemnification and in the checks which had been issued to him as payee and delivered to his bank in Cuba.

It is not necessary, for the purposes of this opinion, to determine whether Alvarez sustained a loss at the time of the taking of his real property in Camaguey, but, if he did then sustain a loss, it was a loss of the difference between his adjusted basis in the property and the value of his right to indemnification. Such loss, if any, would play no part in the computation of any income taxes pay-

[1]See 26 U.S.C.A. § 873; Treas. Reg. 1.871-1; David Schnur v. Commissioner, 10 T.C. 208; Houdry v. Commissioner, 7 T.C. 666.

able to the United States since it occurred prior to the time in which Alvarez became a resident alien.[4]

The controlling issue on this appeal is whether Alvarez sustained a loss by reason of the confiscation of the unused checks and the remaining value of his right of indemnification resulting from Law No. 989; and, if he did thereby sustain a loss, was it a trade or business loss under Section 165(c) entitling him to have such loss allowed in the computation of his tax liability for 1961 and the subsequent carryover years.[5] Alvarez had property and property rights in Cuba after becoming a resident alien and before the effective date of Law No. 989. There can be no doubt that this law divested him of his property and property rights, resulting in a loss to him.

At the time when the Cuban Government took the rented real property of Alvarez, he was divested of trade or business property and for this property there was substituted the non-interest bearing obligation of the Cuban Government. There was a conversion of one kind of property into that of another kind. All of the charac-

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[4]Id.

[5]It should be noted that for Alvarez to receive any tax benefit by way of a deduction and carryover of his loss, the loss must be characterized as one incurred in his trade or business. The loss cannot be deducted under Section 165(c)(3) of the Code because the Internal Revenue Service has taken the position, and the Tax Court has agreed, that, in the absence of special legislation, a loss by way of confiscation under color of legal authority is neither a casualty nor a theft. William J. Powers v. Commissioner, 36 T.C. 1191, I.T. 4086, 1952-1 Cum. Bull. 29. Similarly, if the loss is characterized as one incurred in a transaction entered into for profit under Section 165(c)(2), a deduction for such loss cannot be a part of a net operating loss carryover. 28 U.S.C.A. § 172(c), (d)(4); Treas. Reg. § 1.172-3(a)(1), (a)(2), and (a)(3)(ii-iii). A Section 165(c)(2) loss may be utilized in determining a "net operating loss" deduction only to the extent of nonbusiness income in the year of loss. 28 U.S.C.A. § 172(d).

teristics of finality were present. No profit could have resulted from the ownership of the right of indemnification. Thus the loss sustained does not meet the profit motive test to qualify it as a trade or business loss. See 5 Mertens, Law of Federal Income Taxation, § 28.31, 130-31. The Cuban promise of indemnification was an obligation for the payment of money, nothing more or less. The obligation received did not have the trade of business attributes of the property for which it was received even though the conversion was involuntary. The trade or business attribute cannot attach to the right of indemnification by the application of a doctrine of relation back to the trade or business property for which the indemnification was given. Situations in which there has been a relation back to prior transactions in earlier tax years to determine the taxable nature of a subsequent transaction have been cases where the subsequent transaction was an amendment or modification of the original one. See **Arrowsmith v. Commissioner**, 344 U.S. 6, 97 L.Ed. 6, 73 S.Ct. 71; **Wener v. Commissioner**, 9th Cir. 1957, 242 F.2d 938; **Commissioner v. Adam, Meldrum & Anderson Company**, 2d Cir. 1954, 215 F.2d 163; **Duveen Brothers, Inc. v. Commissioner**, 2d Cir. 1952, 197 F.2d 118. Here, the confiscation of the right of indemnification and other intangibles was related to the earlier taking only in that the fruit of the first was the subject of the second. This is not enough. The 1961 law did not in any way amend, modify, or even relate to the earlier law. Rather, Law No. 989 spoke to a different situation, namely, the property of Cuban absentees.

It is contended by Alvarez that the taking of his real estate by the Cuban Government in 1960 and the giving to him of a right of indemnification constituted an install-

ment sale and that he was entitled to treat the confiscation of his right of indemnification as a loss under Section 453(d)(1).[6] It is doubtful that the taking of Alvarez' property could be regarded as an installment sale within the meaning of the provision of the Code. But, whether so or not, Alvarez did not bring himself within the provisions of Section 453 through compliance with the election requirement of that statute, **Marcello v. Commissioner**, 5th Cir. 1967, 380 F.2d 499, cert. den. 389 U.S. 1044, 19 L.Ed.2d 835, 88 S.Ct. 787. The taxpayer's contention is plausible, but we think it must be rejected.

We are aware of decisions by other courts involving questions similar to those which are here presented,[7] including a case in which it was held that losses similar to that sustained by Alvarez are trade or business losses.[8] However, the conclusion that a loss such as was sustained

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[6]"(d) Gain or loss on disposition of installment obligations. —

(1) General rule. — If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and —

(a) the amount realized, in the case of satisfaction at other than face value or a sale or exchange, or

(b) the fair market value of the obligation at the time of distribution, transmission, or disposition, in the case of distribution, transmission, or disposition otherwise than by sale or exchange.

Any gain or loss so resulting shall be considered as resulting from the sale or exchange of the property in respect of which the installment obligation was received."

26 U.S.C.A. § 453(d)(1).

[7]Luis Bosch v. Commissioner, T.C. Mem. 1970-66; Vila v. United States, S.D. Fla.1969, 301 F.Supp. 1004; Garrigo v. United States, N.D. Tex.1968, 296 F.Supp. 1110.

[8]Beltran v. Commissioner, 69-2 USTC 85,752. Appeal pending, 7th Cir.

by Alvarez is a trade or business loss is not the better view. We believe that a contrary result must be reached. The case of Luis Bosch, now pending on appeal before this Court,[1] involves a somewhat different issue than is presented by this case.

Since we decide this case, which seems to be one of first impression in this Court, on the ground that the right of indemnification was not property held for trade of business, it is unnecessary to give consideration to the other questions presented. The judgment of the district court will be reversed and cause remanded for entry of an appropriate judgment in keeping with this opinion.

REVERSED AND REMANDED.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

No. 68-1-Civ-EC

CESAR E. ALVAREZ and ANA I. ALVAREZ,
Plaintiffs,

vs.

UNITED STATES OF AMERICA,
Defendant.

Filed June 27, 1969

[1]Bosch v. C.I.R. No. 30152, 5th Cir., July 20, 1970.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

This cause came on for trial pursuant to due notice and upon consideration of the evidence presented to the court without a jury and upon memoranda of law, pretrial stipulation, and argument of counsel, the court finds as follows:

FINDINGS OF FACT

1. This is an action brought by the plaintiffs for the refund of income taxes for the taxable years 1962 and 1963. For each of these years, the plaintiffs timely filed income tax returns and paid income taxes of Sixty-five dollars ($65.00) in 1962 and Four hundred sixteen dollars ($416.00) in 1963. On December 28, 1964, the plaintiffs claimed a refund for the sum of Four hundred sixteen dollars ($416.00) and on April 11, 1966, a refund claim was filed for the year 1962 in the amount of Sixty-five dollars ($65.00). Both claims were filed on Government Form 843. On January 25, 1966, the claim for refund for 1963 was denied with full disallowance and on November 16, 1966, the claim for refund for 1962 was denied with full disallowance and this suit followed.

All jurisdictional prerequisites to bring this suit have been met, and this court has jurisdiction over the parties and the subject matter of this litigation.

2. The basis for recovery, as claimed by the plaintiffs, is an operating loss totaling Thirty-five thousand dollars ($35,000.00), by virtue of the expropriation of the plaintiffs' business property by Cuban Government under

Law #989, enacted on December 5, 1961. Law #989 provided for total confiscation without compensation of all properties owned by Cuban Nationals who had left Cuba. Plaintiffs alternatively claim the loss of the right to receive indemnification as provided by the law of Urban Reform of October 14, 1960, in the amount of Twenty-two thousand four hundred dollars ($22,400.00). The plaintiffs received compensation for eight months before leaving Cuba, leaving the balance due, to which plaintiffs would have been entitled under the Urban Reform Law, of nine years, four months, at Two Hundred dollars ($200.00) per month, or Twenty-two thousand four hundred dollars ($22,400.00).

3. The plaintiffs timely filed a joint income tax return for the calendar year 1961, showing One thousand one hundred sixty-nine dollars ($1,169.00) in gross receipts or gross income and no tax being due or owing.

4. Mr. Cesar Alvarez departed Cuba and entered into the United States on June 6, 1961. Mr. Alvarez became a resident alien of the United States and a United States taxpayer on July 6, 1961, when he declared his intention to stay in the United States and not to return under the visitor's permit with which he had originally entered the country on June 6, 1961.

5. On October 14, 1960, the Revolutionary Government of Cuba enacted the Urban Reform Law. By virtue of the Urban Reform Law, the Cuban Government intervened all urban rental property in Cuba and promised indemnification to the owners and further gave occupying tenants the right to purchase ownership of their apartments by installment payments, contingent on the tenant's

declaration of intent. If a tenant made all the requisite payments, then the tenant would obtain an interest in the property. Said interest did not include the right to convey the interest without approval of the Cuban Government. Plaintiffs' property, located at Avenita des los Martierez No. 66, Comaquez, Cuba, was subject to the provisions of this law. When Mr. Alvarez temporarily left Cuba on June 6, 1961, he did not sustain a loss at that time since the loss was not reasonably certain in fact, and was not ascertainable in amount as a practical matter and in view of a realistic appraisal of all the facts and circumstances as of June 6, 1961. As of that time the Urban Reform Law had only been enacted for a period of approximately eight months. The plaintiffs herein had chosen to receive payments as offered under said Urban Reform Law and had been receiving payments from October 31, 1960, through May 31, 1961, in the amount of Two hundred dollars ($200.00) per month. Thus, the Urban Reform Law, in effect, took nothing from plaintiff and was indemnifying him under his right as claimed by him for property which might sometime in the future become that of anoth but which property, until and including the time of his departure, was still titled in his name.

6. The plaintiff herein chose to temporarily leave Cuba because of the unstable political climate. He had left Cuba many times before to visit his family who lived in the United States, but had always returned to his business in Cuba. Thus, he did not leave because of economic reasons, and had fully intended to return to Cuba. He had every reasonable expectation to be indemnified for the property in Cuba as he was receiving said indemnification and therefore, under Treasury Regulations 1.165-1-(d) (1) and 1.165-1-(d) (2) (i) a loss had not occurred. The facts

of this case indicate that the plaintiffs were reasonable in their expectation that their indemnification which they were receiving for their property as of October 14, 1960, would continue. Their loss took place on December 5, 1961, by virtue of Cuban Statute 989, which confiscated their property without indemnification.

7. The plaintiffs have proven by a preponderance of the evidence that they have suffered a loss from the confiscation of business property located at Avenita de los Martierez No. 66 (Avenue of the Martierez No. 66) Comaguez, Cuba, with a land value of Twenty thousand dollars ($20,000.00) and a building (parking garage and stores) value of Fifty thousand dollars ($50,000.00), for a total loss of Seventy thousand dollars ($70,000.00), of which the plaintiffs owned a one-half interest. Plaintiffs have further proven by a preponderance of the evidence that this property was property used in their trade or business, and that its confiscation resulted in an operating loss under Sections 165(c)(1) and 172(c) and that such loss can be carried forward ten years pursuant to Section 172(b)(1)(D), since they have elected under Section 172(b)(c)(iii).

8. Plaintiff's testimony was believable and uncontradicted and was further corroborated by evidence acquired from the Cuban Judicia, which showed plaintiff was receiving rent on the property in question for Four hundred dollars ($400.00) per month, of which his interest was one-half, which substantiates the fact that plaintiff was entitled to Two hundred dollars ($200.00) per month recompense for the taking of his property in accordance with Cuban Urban Reform Law.

CONCLUSIONS OF LAW

9. For Federal Income Tax purposes, alien individuals are divided generally into two classes, resident aliens and non-resident aliens. Resident aliens are in general taxable in the same manner as citizens of the United States. Treas. Reg. § 1.871-1. The fact that a taxpayer entered the United States on a visitor's visa is not a persuasive indication of his intention at that time, since he was then unable to obtain any other type of visa. Plaintiff was a resident alien at the time the loss occurred. Revenue Ruling 62-197.

10. The plaintiffs did not abandon their property. Abandonment must be clearly proven and the burden of proof is on the party claiming abandonment. It must affirmatively appear that the property or right alleged to have been abandoned has been relinquished by its owner or holder with the intention of abandoning it and with no intention of returning to or reclaiming it.

11. The Internal Revenue Service has recognized that when a person flees a country he does not usually have the time to take with him all of the evidence of ownership. In *Peter v. Elek*, 30 T.C. 731 (1958), the court held that one must use the best available evidence. In *Andrew v. Solt*, 19 T.C. 183 (1952), the Tax Court has applied a reasonable estimate of adjusted basis, citing the familiar Cohan Rule (*Cohan v. Commissioner*, 39 F.2d 540 (2 Cir. 1930)). In the recent case of *Alvary v. United States*, 302 F.2d 790 (2 Cir. 1962), the government conceded that the expropriated property had some value but merely challenged the taxpayer's estimate without offering any of its own evidence. The Court accepted the taxpayer's estimate.

The fact that a plaintiff relies on his own testimony to support his contention in a case does not render the evidence insufficient as a matter of law. *Winter Haven Fruit Sales Corp. v. De Vane*, 120 Fla. 385, 162 So. 909 (1935). Evaluation of evidence is primarily the function of the trier of fact.

12. Losses sustained by an individual are deductible if they are incurred either in his trade or business or in a transaction entered into for profit though not connected with his trade or business. Internal Revenue Code 165(c). Plaintiffs loss, insofar as it resulted from the taking of his right to indemnification, is a loss from the sale or exchange of property in respect of which the right to payment was received. In other words, the character of the loss stems from the nature and character of the asset from which the right to indemnification arose. A close analogy is a loss sustained with respect to an installment obligation, the character of which is derived from the sale or exchange of property in respect of which the installment obligation was received. Internal Revenue Code § 453(d)(1), Treas. Reg. 1.453-9(a).

13. The plaintiffs are entitled to a deduction for loss under Section 165, because they have proved by a preponderance of the evidence:

(a) That they owned the property for which the loss is claimed.

(b) That they did not sustain the loss on the property at or before the time of their departure from Cuba on June 6, 1961.

(c) That they were resident aliens of the United States at the time the property was expropriated.

(d) That the expropriated property was property used in their trade or business, and

(e) That the amount of the loss, which is the adjusted basis of the property at the date the loss occurred, as defined in Section 165(b), converted into United States currency, was Thirty-five Thousand Dollars ($35,000.00).

14. The plaintiffs have established their adjusted basis and are entitled to a business loss which may be carried back and carried forward as a net operating loss in accordance with the provisions of Internal Revenue Code §§ 165, 172, and 1231.

15. Depreciation is not a factor in the instant case. The Court takes judicial notice that any depreciation on this structure allowed or allowable on a straight line basis over a term of fifty years would not reduce the basis of the property below the amount of indemnification plaintiff was to receive from the Cuban Government.

16. Any finding of fact hereinabove made which also constitutes a conclusion of law is adopted as a conclusion of law and any conclusion of law hereinabove made which also constitutes a finding of fact is adopted as a finding of fact.

Counsel for the Plaintiffs is hereby directed to submit an appropriate judgment in conformity with this opinion within five (5) days of the date of the entry hereof.

DONE and ORDERED at Miami, Florida, on this 20th day of June, 1969.

EMETT C. CHOATE

SENIOR UNITED STATES DISTRICT JUDGE

In the Supreme Court of the United States

OCTOBER TERM, 1970

No. 1011

CESAR E. ALVAREZ AND ANA I. ALVAREZ, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The findings of fact and conclusions of law of the district court (Pet. App. 9–17) are not reported. The opinion of the court of appeals (Pet. App. 2–9) is reported at 431 F. 2d 1261.

JURISDICTION

The judgment of the court of appeals was entered on September 1, 1970 (Pet. App. 1–2). The petition for a writ of certiorari was filed on November 27, 1970. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

412-475—70

QUESTION PRESENTED

Whether the Cuban Government's confiscation in 1961 of an indemnification right, which had been previously granted to petitioner upon the seizure of his rental realty, resulted in a trade or business loss which may be carried over and deducted in subsequent years under Section 172 of the Internal Revenue Code of 1954.

STATUTES AND REGULATIONS INVOLVED

The pertinent provisions of Sections 165 and 172 of the Internal Revenue Code of 1954 and of Sections 1.165–1 and 1.172–3 of the Treasury Regulations on Income Tax (1954 Code) are set forth in the Appendix, *infra*, pp. 9–16.

STATEMENT

Petitioner,[1] a Cuban citizen, owned an undivided half-interest in improved business realty in Cuba, which was rented to a number of tenants. The Cuban Government seized the property under the Urban Reform Law promulgated on October 14, 1960, which provided a limited indemnification right for former owners. Petitioner was given a nontransferable indemnification right of $22,400, payable at the rate of $200 per month for nine years and four months. He received eight payments prior to his final departure from Cuba on June 6, 1961. (Pet. App. 3, 5.)

On December 5, 1961, the Cuban Government promulgated "Law No. 989" confiscating all property

[1] References to "petitioner" are to Cesar E. Alvarez. Ana I. Alvarez is a party hereto only because joint income tax returns were filed for the years in issue.

rights of Cubans who failed to return to Cuba within a designated time unless they received permission to remain outside of Cuba. Since petitioner did not return to Cuba or receive permission from the Cuban Government to remain absent from Cuba, his indemnification right was confiscated. (Pet. App. 4.)

The district court held that petitioner, for tax purposes, suffered the loss of his rental property on December 5, 1961, the enactment date of "Law No. 989," and that the loss was a business loss which could be carried over to 1962 and 1963 under Section 172 of the Internal Revenue Code (Pet. App. 10–17). On appeal, the Fifth Circuit reversed. It held that after promulgation of the Urban Reform Law of October 14, 1960, petitioner had only the right to indemnification, a nonbusiness asset (Pet. App. 5), and that the loss of this indemnification right in December, 1961, was a nonbusiness loss which could not be carried forward to 1962 and 1963 under the net operating loss carryover provisions of Section 172 (Pet. App. 6–8).[2]

[2] The government submits that both the district court and the court of appeals erred as a matter of law in concluding that petitioner's indemnification right had any value to him after he became a resident alien. A taxpayer has the burden of proof to establish that he lost something of value, for which a deduction is allowable in the year it is claimed. *Boehm* v. *Commissioner*, 326 U.S. 287, 294; *James Petroleum Corp.* v. *Commissioner*, 238 F. 2d 678, 679–680 (C.A. 2). Petitioner failed to meet that burden. He testified that he had to be present in Cuba to receive the checks, and he stated that he would not go back to Cuba so long as Castro was in power. The value of his indemnification right to him thus turned upon unforeseen political events, and could not be proved. The judgment of the court of appeals could be sustained for this reason alone.

ARGUMENT

The decision below is correct. There is no conflict of decisions among the circuits or any other reason for further review by this Court.

1. The court of appeals correctly held that the loss was not a business loss deductible under Section 165 (c)(1) (Appendix, *infra*, p. 9) which could be carried forward under Section 172(a) (Appendix, *infra*, pp. 9–10). Before entering this country, petitioner had involuntarily exchanged his business realty for an indemnification right and after October 14, 1960, held only a right of indemnification. See *Hawaiian Gas Products* v. *Commissioner*, 126 F. 2d 4 (C.A. 9). That right was a nonbusiness asset separate and distinct from the property for which it had been given. The amount to be received from the Cuban Government for the seizure of the property was neither speculative nor indeterminate while petitioner remained in Cuba. In fact, petitioner did receive payments in accordance with the provisions of the Urban Reform Law when he was in Cuba.

The confiscation of the indemnification right on December 5, 1961, was unrelated to the seizure on October 14, 1960, and, therefore, the character of the loss suffered on December 5, 1961, cannot be determined by reference to the character of the realty seized on Octo-

ber 14, 1960.[a] There is no evidence that petitioner had a business in which he dealt in indemnification rights. Accordingly, petitioner's loss on December 5, 1961, of his indemnification right was not deductible as a business loss under Section 165(c)(1). Since nonbusiness losses may be utilized in determining a "net operating loss" deduction only to the extent of the nonbusiness income in the year of loss, there can be no carryover to the years in suit. See Section 172(d)(4) of the Internal Revenue Code, Appendix, *infra*, p. 11; Section 1.172–3(a)(3) of the Treasury Regulations on Income Tax (1954 Code), Appendix, *infra*, pp. 15–16.

Section 1.165–1(d)(2) of the Treasury Regulations

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[a] The situation here is distinguishable from that in *Arrowsmith* v. *Commissioner*, 344 U.S. 6. There, the loss involved stemmed from a judgment against a liquidated corporation. Had the judgment been paid by the corporation prior to its liquidation, the loss would have been a capital loss. This Court held that the mere fact that it was paid by the transferees of the corporation's assets several years after the corporation's liquidation did not change the character of the loss. The taking of petitioner's indemnification right on December 5, 1961, did not relate back to the taking of the realty on October 14, 1960. "Law No. 989" in no way modified the Urban Reform Law. If it had modified that law, an *Arrowsmith* situation would have arisen. But "Law No. 989" addressed itself to a different situation, namely to property of those Cubans who had left Cuba. Petitioner's situation in substance is no different than if he had received a promissory note for the purchase of his business realty. The exchange of the realty for the note would have constituted a taxable transaction for federal tax purposes. If the government then had seized his note, the characterization of the loss would not have been determined by reference to the transaction in which he received the note.

on Income Tax (1954 Code), Appendix, *infra*, pp. 12–14, cited by petitioner (Pet. 10), has no bearing on this case. That section of the Regulations and the example therein merely stand for the proposition that as long as a claim with respect to an otherwise deductible loss is in dispute, no deduction can be taken to the extent that there exists a reasonable prospect of recovery of the loss. But once the loss becomes fixed and final, as did petitioner's loss on his realty on October 14, 1960, there is no basis for characterizing a subsequent unrelated loss by reference to the character of the earlier loss.

The court of appeals properly rejected petitioner's claim under Section 453(d)(1) of the Code, which deals with the taxation of income from installment obligations (Pet. App. 7–8). This special section provides that the gain or loss upon the sale or exchange of an installment obligation is to be considered as resulting from the sale or exchange of the property for which the installment obligation was received. It is applicable only if a taxpayer makes a special election. See Treasury Regulations on Income Tax (1954 Code), Section 1.453–8(b); Rev. Rul. 65–297, 1965–2 Cum. Bull. 152. Petitioner made no such election.

Petitioner's claim (Pet. 8) that the court of appeals would "transform a business asset into a nonbusiness asset where a claim for compensation comes into existence" has no merit. Although he argues that the decision below is without statutory, judicial, or ad-

ministrative support (Pet. 8), he fails to cite any contrary authority.

2. While the issue here is presented in some 1,300 cases pending administratively and in the courts, involving over $3,000,000 in taxes, it is not ripe for review by this Court at this time. Petitioner admits that there is no conflict in the circuits, but relies on the district court's decisions in the consolidated cases of *Beltran* v. *United States* and *Onetti* v. *United States,* 69–2 U.S.T.C., par. 9649 (D.C. Ill.), now pending on appeal in the Seventh Circuit (Pet. 10). Unless the Seventh Circuit affirms *Beltran* and *Onetti,* thereby creating a conflict, there is no basis for review here.

CONCLUSION

The petition for a writ of certiorari should be denied. Alternatively, action on the petition should be deferred pending disposition of the *Beltran* and *Onetti* cases.

Respectfully submitted.

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DECEMBER 1970.

APPENDIX

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 165. LOSSES.

(a) *General Rule.*—There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.

(b) *Amount of Deduction.*—For purposes of subsection (a), the basis for determining the amount of the deduction for any loss shall be the adjusted basis provided in section 1011 for determining the loss from the sale or other disposition of property.

(c) *Limitation on Losses of Individuals.*—In the case of an individual, the deduction under subsection (a) shall be limited to—

(1) losses incurred in a trade or business;

(2) losses incurred in any transaction entered into for profit, though not connected with a trade or business; and

(3) losses of property not connected with a trade or business, if such losses arise from fire, storm, shipwreck, or other casualty, or from theft. No loss described in this paragraph shall be allowed if, at the time of the filing of the return, such loss has been claimed for estate tax purposes in the estate tax return.

* * * * *

SEC. 172 [as amended by Sec. 317(b), Trade Expansion Act of 1962, P.L. 87-794, 76 Stat. 872, and by Sec. 210(a), Revenue Act of 1964, P.L. 88-272, 78 Stat. 19]. NET OPERATING LOSS DEDUCTION.

(a) *Deduction Allowed.*—There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (1) the net

operating loss carryovers to such year, plus (2) the net operating loss carrybacks to such year. For purposes of this subtitle, the term "net operating loss deduction" means the deduction allowed by this subsection.

(b) *Net Operating Loss Carrybacks and Carryovers.*—

(1) *Years to which loss may be carried.*—

* * * * *

(D) In the case of a taxpayer which has a foreign expropriation loss (as defined in subsection (k) for any taxable year ending after December 31, 1958, the portion of the net operating loss for such year attributable to such foreign expropriation loss shall not be a net operating loss carryback to any taxable year preceding the taxable year of such loss and shall be a net operating loss carryover to each of the 10 taxable years following the taxable year of such loss.

* * * * *

(c) *Net Operating Loss Defined.*—For purposes of this section, the term "net operating loss" means (for any taxable year ending after December 31, 1953) the excess of the deductions allowed by this chapter over the gross income. Such excess shall be computed with the modifications specified in subsection (d).

(d) *Modifications.*—The modifications referred to in this section are as follows:

(1) *Net operating loss deduction.*—No net operating loss deduction shall be allowed.

(2) *Capital gains and losses of taxpayers other than corporations.*—In the case of a taxpayer other than a corporation—

(A) the amount deductible on account of losses from sales or exchanges of capital assets shall not exceed the amount includible on account of gains from sales or exchanges of capital assets; and

(B) the deduction for long-term capital gains provided by section 1202 shall no be allowed.

(3) *Deduction for personal exemptions.*—No deduction shall be allowed under section 151 (relating to personal exemptions). No deduction in lieu of any such deduction shall be allowed.

(4) *Nonbusiness deductions of taxpayers other than corporations.*—In the case of a taxpayer other than a corporation, the deductions allowable by this chapter which are not attributable to a taxpayer's trade or business shall be allowed only to the extent of the amount of the gross income not derived from such trade or business. For purposes of the preceding sentence—

(A) any gain or loss from the sale or other disposition of—

(i) property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 167, or

(ii) real property used in the trade or business,

shall be treated as attributable to the trade or business;

(B) the modifications specified in paragraphs (1), (2)(B), and (3) shall be taken into account; and

(C) any deduction allowable under section 165(c)(3) (relating to casualty losses) shall not be taken into account.

* * * * * *

Treasury Regulations on Income Tax (1954 Code) (26 C.F.R.):

§ 1.165–1 *Losses.*

(a) *Allowance of deduction.* Section 165(a) provides that, in computing taxable income under section 63, any loss actually sustained during the taxable year and not made good by insurance or some other form of compensa-

tion shall be allowed as a deduction subject to any provision of the internal revenue laws which prohibits or limits the amount of the deduction. This deduction for losses sustained shall be taken in accordance with section 165 and the regulations thereunder. For the disallowance of deductions for worthless securities issued by a political party, see § 1.271–1.

(b) *Nature of loss allowable.* To be allowable as a deduction under section 165(a), a loss must be evidenced by closed and completed transactions, fixed by identifiable events, and, except as otherwise provided in section 165(h) and § 1.165–11, relating to disaster losses actually sustained during the taxable year. Only a bona fide loss is allowable. Substance and not mere form shall govern in determining a deductible loss.

(c) *Amount deductible.* (1) The amount of loss allowable as a deduction under section 165 (a) shall not exceed the amount prescribed by § 1.1011–1 as the adjusted basis for determining the loss from the sale or other disposition of the property involved. In the case of each such deduction claimed, therefore, the basis of the property must be properly adjusted as prescribed by § 1.1011–1 for such items as expenditures, receipts, or losses, properly chargeable to capital account, and for such items as depreciation, obsolescence, amortization, and depletion, in order to determine the amount of loss allowable as a deduction. To determine the allowable loss in the case of property acquired before March 1, 1913, see also paragraph (b) of § 1.1053–1.

* * * * *

(d) *Year of deduction.* (1) A loss shall be allowed as a deduction under section 165(a) only for the taxable year in which the loss is sustained. For this purpose, a loss shall be treated as sustained during the taxable year in which the loss occurs as evidenced by closed and com-

pleted transactions and as fixed by identifiable events occurring in such taxable year. For provisions relating to situations where a loss attributable to a disaster will be treated as sustained in the taxable year immediately preceding the taxable year in which the disaster actually occurred, see section 165(h) and § 1.165–11.

(2)(i) If a casualty or other event occurs which may result in a loss and in the year of such casualty or event, there exists a claim for reimbursement with respect to which there is a reasonable prospect of recovery, no portion of the loss with respect to which reimbursement may be received is sustained, for purposes of section 165, until it can be ascertained with reasonable certainty whether or not such reimbursement will be received. Whether a reasonable prospect of recovery exists with respect to a claim for reimbursement of a loss is a question of fact to be determined upon an examination of all facts and circumstances. Whether or not such reimbursement will be received may be ascertained with reasonable certainty, for example, by a settlement of the claim, by an adjudication of the claim, or by an abandonment of the claim. When a taxpayer claims that the taxable year in which a loss is sustained is fixed by his abandonment of the claim for reimbursement, he must be able to produce objective evidence of his having abandoned the claim, such as the execution of a release.

(ii) If in the year of the casualty or other event a portion of the loss is not covered by a claim for reimbursement with respect to which there is a reasonable prospect of recovery, then such portion of the loss is sustained during the taxable year in which the casualty or other event occurs. For example, if property having an adjusted basis of $10,000 is completely destroyed by fire in 1961, and if the taxpayer's only claim for reimbursement consists of an insurance

claim for $8,000 which is settled in 1962, the taxpayer sustains a loss of $2,000 in 1961. However, if the taxpayer's automobile is completely destroyed in 1961 as a result of the negligence of another person and there exists a reasonable prospect of recovery on a claim for the full value of the automobile against such person the taxpayer does not sustain any loss until the taxable year in which the claim is adjudicated or otherwise settled. If the automobile had an adjusted basis of $5,000 and the taxpayer secures a judgment of $4,000 in 1962, $1,000 is deductible for the taxable year 1962. If in 1963 it becames reasonably certain that only $3,500 can ever be collected on such judgment, $500 is deductible for the taxable year 1963.

* * * * *

§ 1.172–3 *Net operating loss in case of a taxpayer other than a corporation.*

(a) *Modification of deductions.* A net operating loss is sustained by a taxpayer other than a corporation in any taxable year beginning after December 31, 1953 if and to the extent that, for such year there is an excess of deductions allowed by chapter 1 of the Internal Revenue Code of 1954 over gross income computed thereunder; this rule shall apply even though the loss year is otherwise subject to the Internal Revenue Code of 1939. In determining the excess of deductions over gross income for such purpose—

(1) *Items not deductible.* No deduction shall be allowed under—

(i) Section 151 for the personal exemptions or under any other section which grants a deduction in lieu of the deductions allowed by section 151.

(ii) Section 172 for the net operating loss deduction, and

(iii) Section 1202 in respect of the net long-term capital gain.

(2) *Capital losses.* (i) The amount deductible on account of business capital losses shall not exceed the sum of the amount includible on account of business capital gains and that portion of nonbusiness capital gains which is computed in accordance with paragraph (c) of this section.

(ii) The amount deductible on account of nonbusiness capital losses shall not exceed the amount includible on account of nonbusiness capital gains.

(3) *Nonbusiness deductions*—(i) *Ordinary deductions.* Ordinary nonbusiness deductions shall be taken into account without regard to the amount of business deductions and shall be allowed in full to the extent, but not in excess, of that amount which is the sum of the ordinary nonbusiness gross income and the excess of nonbusiness capital gains over nonbusiness capital losses. See paragraph (c) of this section. For purposes of section 172, nonbusiness deductions and income are those deductions and that income which are not attributable to, or derived from, a taxpayer's trade or business. Wages and salary constitute income attributable to the taxpayer's trade or business for such purposes.

(ii) *Sale of business property.* Any gain or loss on the sale or other disposition of property which is used in the taxpayer's trade or business and which is of a character that is subject to the allowance for depreciation provided in section 167, or of real property used in the taxpayer's trade or business, shall be considered, for purposes of section 172(d)(4), as attributable to, or derived from, the taxpayer's trade or business. Such gains and losses are to be taken into account fully in computing a net operating loss without regard to the limitation on nonbusiness deductions. Thus, a farmer who sells at a loss land used in the business of farming may

in computing a net operating loss, include in full the deduction otherwise allowable with respect to such loss, without regard to the amount of his nonbusiness income and without regard to whether he is engaged in the trade or business of selling farms. Similiarly, an individual who sells at a loss machinery which is used in his trade or business and which is of a character that is subject to the allowance for depreciation may, in computing the net operating loss, include in full the deduction otherwise allowable with respect to such loss.

(iii) *Casualty losses.* Any deduction allowable under section 165(c)(3) for losses of property not connected with a trade or business shall not be considered, for purposes of section 172 (d)(4), to be a nonbusiness deduction but shall be treated as a deduction attributable to the taxpayer's trade or business.

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U.S. GOVERNMENT PRINTING OFFICE 9-10